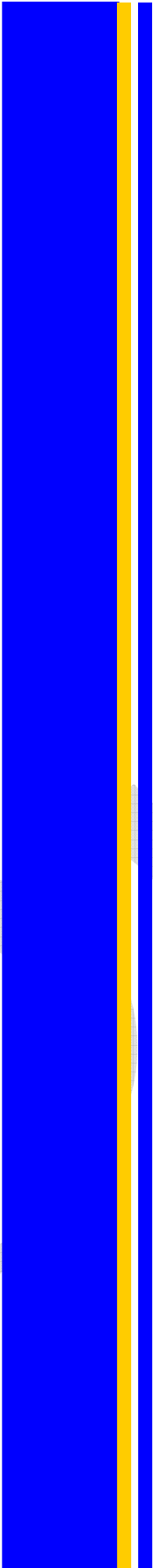




# **FEDERAL HOUSING FINANCE BOARD**

## **FY2007-2012 STRATEGIC PLAN**

**AUGUST 31, 2006**



*The Federal Housing Finance Board's strategic plan for fiscal years 2007-2012 is prepared in accordance with the Government Performance and Results Act of 1993. The plan sets out the Finance Board's mission, vision, values, and strategic goals for the next five years. The plan also identifies the initiatives the Finance Board will undertake to achieve its goals, its performance outcomes, and performance measures to monitor achievement of those goals.*

*Direct comments on this plan to:*  
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# TABLE OF CONTENTS

	<u>Page</u>
MESSAGE FROM THE CHAIRMAN.....	1
INTRODUCTION.....	3
MISSION, VISION, AND VALUES .....	6
STRATEGIC GOALS.....	7
MEANS AND STRATEGIES.....	8
STRATEGIC GOALS AND ANNUAL PERFORMANCE GOALS .....	
GOAL 1: THE FEDERAL HOME LOAN BANKS OPERATE SAFELY AND SOUNDLY.	10
GOAL 2: THE FEDERAL HOME LOAN BANKS SERVE THE NATION'S HOUSING FINANCE AND COMMUNITY INVESTMENT NEEDS.	11
KEY EXTERNAL FACTORS .....	13
STRATEGIC PLANNING PROCESS.....	15
PROGRAM EVALUATION.....	16

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## MESSAGE FROM THE CHAIRMAN

On behalf of the board of directors, I am pleased to present the Federal Housing Finance Board (Finance Board) Strategic Plan (Plan) for fiscal years 2007-2012. The Plan establishes the Finance Board's strategic direction by defining the agency's vision, goals, and strategies for the next five years. In establishing its goals and implementing its strategies, the Finance Board is mindful of its primary duty to ensure that the Federal Home Loan Banks (FHLBanks) operate in a financially safe and sound manner, and its other duties to supervise the FHLBanks, to ensure that they carry out their housing finance mission and that they remain adequately capitalized and able to raise funds in the capital markets. In carrying out its duties the Finance Board will:

- Execute an effective, risk-based supervisory and regulatory program to promptly identify and address current and emerging risks to the FHLBanks. In fiscal year 2007, the Finance Board will implement a risk rating system;
- Advance community and economic development activities of the FHLBanks through an oversight program and responsive regulation; and
- Maximize agency effectiveness by aligning resources with supervisory responsibilities and continuing to enhance its information technology infrastructure.

The Finance Board will continue to supervise the FHLBanks to maintain a strong FHLBank System. We will monitor our progress and performance on the initiatives outlined in this Plan and respond appropriately.

Above all, by fulfilling the mission reflected in this Plan, the vision and values of the Finance Board will effectively serve the public who depend upon the FHLBanks as an integral part of the nation's housing finance system.

Ronald A. Rosenfeld  
Chairman

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## INTRODUCTION

### FEDERAL HOUSING FINANCE BOARD

In 1989, Congress established the Finance Board as an independent executive agency to succeed to the authority of the former Federal Home Loan Bank Board with respect to the FHLBanks. The law establishing the Finance Board and prescribing the powers and duties of the Finance Board and the FHLBanks is the Federal Home Loan Bank Act (FHLBank Act). The primary duty of the Finance Board is to ensure that the FHLBanks operate in a financially safe and sound manner. Consistent with ensuring the safe and sound operations of the FHLBanks, the Finance Board will also carry out its other statutory duties of the Finance Board: to supervise the FHLBanks, to ensure that the FHLBanks carry out their housing finance mission, and to ensure the FHLBanks remain adequately capitalized and able to raise funds in the capital markets.

The Finance Board is funded by assessments on the twelve FHLBanks. It receives no appropriations, and its funds are not Government monies.

### ORGANIZATION

The FHLBank Act vests stewardship of the Finance Board in a five-member board of directors consisting of four members appointed by the President with the advice and consent of the Senate and one *ex officio* member, the Secretary of the Department of Housing and Urban Development. No more than three directors may be from the same political party. The appointed directors must have experience or training in housing finance or a commitment to providing specialized housing credit. At least one director must be from an organization with more than a two-year history of representing consumer or community interests in banking services, credit needs, housing, or financial consumer protections. The directors serve staggered seven-year terms. The President designates the chairperson from among the appointed members.

The Finance Board is organized into five Offices:

The Office of the Board of Directors is responsible for setting the agency's overall strategic direction, and approving policies and regulations. By delegation from the full board of directors, the Chairman supervises management and policy execution. The Board of Directors generally meets monthly in public sessions. The agency's Chief Information Officer, who is responsible for the Finance Board's technology and information systems reports to the Chairman.

The Office of Supervision (OS) is responsible for the supervision and examination of the FHLBanks and the Office of Finance (OF). OS performs this function through annual on-site examinations, quarterly visitations and off-site monitoring of the FHLBanks and OF. Other responsibilities of OS include supervisory policy and program development, regulatory analysis and development, and economic research and analysis.

The *Office of General Counsel* (OGC) provides legal support and guidance on interpretations of laws, regulations, and policies to Finance Board officials. The OGC prepares all legal documents on behalf of the Finance Board and represents the agency in judicial and administrative proceedings. OGC staff manages the Finance Board's ethics, FOIA, and privacy programs.

The Office of Management (OM) is responsible for the Finance Board's administrative functions, such as accounting, budgeting, human resources, contracting and procurement, facilities and property management, and records management.

The *Office of Inspector General* (OIG) operates pursuant to the Inspector General Act of 1978, as amended. The OIG conducts and supervises audits and investigations related to agency programs and operations, and recommends policies for Finance Board programs and operations to promote economy, efficiency, and effectiveness, and to prevent and detect fraud and abuse.

## FEDERAL HOME LOAN BANKS

In 1932, Congress authorized the establishment of the FHLBanks to stimulate mortgage finance and provide liquidity to credit markets. Until 1989, members of the FHLBanks consisted primarily of savings and loan associations engaged in home financing.

The 12 FHLBanks are currently located in Boston, New York, Pittsburgh, Atlanta, Cincinnati, Indianapolis, Chicago, Des Moines, Dallas, Topeka, San Francisco, and Seattle. As of June 30, 2006, the FHLBanks had combined assets exceeding one trillion dollars.

In 1989 Congress extended eligibility for FHLBank membership to commercial banks and to federally insured credit unions (subject to a home financing requirement). At that time, Congress also established several FHLBank community investment programs. In 1999, Congress repealed the mandatory membership requirement for federal savings associations, and made FHLBank membership voluntary for all types of eligible institutions.

The FHLBanks are privately capitalized, government-sponsored enterprises, each with their own management and board of directors. The members of each FHLBank elect a majority of the directors to serve on the board, and the Finance Board appoints a minority of the directors. The FHLBank Act requires that at least two of the appointed directors at each FHLBank be chosen from organizations with more than a two-year history of representing consumer or community interests on banking services, credit needs, housing, or financial consumer protections.

The FHLBanks provide wholesale credit to members and certain nonmembers, principally housing finance agencies, to be used for mortgage lending and related activities. In addition, the FHLBanks have a mandate to promote housing and community investment finance. The FHLBanks provide long-term, flexible financing to more than 8,000 member financial institutions throughout the country.



The FHLBanks are funded principally by the issuance of consolidated obligations of the FHLBank System in the public capital markets through the OF, which acts as the FHLBanks' agent. Debt issued by the FHLBanks through the OF is the joint and several obligation of all 12 FHLBanks. Consolidated obligations of the FHLBank System consist of bonds (original maturity of one year or longer) and discount notes (original maturity of less than one year). Consolidated obligations are not guaranteed or insured by the federal government. However, the FHLBanks' government sponsored enterprise status accords certain privileges and enables the FHLBanks to raise funds at rates just slightly above comparable obligations issued by the U.S. Department of the Treasury.

Only FHLBank members and housing associates (principally state and local housing finance agencies) can borrow from an FHLBank. The benefits of membership flow through access to low-cost funds known as advances (collateralized loans), which a member uses principally to fund mortgage loans and to maintain liquidity for its operations, as well as through dividends paid on member-owned capital stock. The preponderance of the collateral supporting advances consists of mortgage assets.

Access to FHLBank advances enables members to hold lesser amounts of low-yielding liquid assets

than they otherwise would need to hold. A member may use long-term advances only to support residential housing finance and, in the case of a community financial institution, to support lending to small businesses, small farms, and small agricultural businesses.

In addition to advances, the FHLBanks purchase qualifying mortgage loans from members under various acquired member asset programs. Under these programs, the FHLBank manages the market risk associated with the loans, while the member bears most of the credit risk (either directly or indirectly through the purchase of mortgage insurance for the loans sold to the FHLBank).

Members have access to a broad array of community investment funds to support affordable housing and community investment activities. The FHLBank Act requires each FHLBank to allocate ten percent of its prior year's net income to fund a subsidy program known as the Affordable Housing Program (AHP). Under the terms of the AHP, a member may submit an application to its FHLBank for funds to be used to finance housing for very low-, low-, and moderate-income households. As of June 30, 2006, the FHLBanks have committed approximately \$\_\_ billion in AHP subsidies to their members since 1990.

## MISSION STATEMENT

## VISION

## VALUES

**MISSION:** The Finance Board's mission is to ensure that the FHLBanks are safe and sound so they serve as a reliable source of liquidity and funding for the nation's housing finance and community investment needs.

**VISION:** To maintain the public's trust, the Finance Board is dedicated to the highest professional standards of accountability and independence to carry out its responsibilities for FHLBank supervision and housing finance mission oversight.

**VALUES:** The core values underlying the Finance Board's mission and vision, and guiding its organizational decisions and actions, are:

- *Independence.* The Finance Board is the arm's-length regulator of the FHLBanks and the OF.
- *Accountability.* The Finance Board is a steward of the public's trust and will use its resources efficiently and in the public interest.
- *Responsiveness.* The Finance Board aligns its actions with its mission and responds promptly, effectively, and appropriately to emerging risks and opportunities in the financial system
- *Integrity.* The Finance Board discharges its responsibilities fairly and impartially and adheres to the highest standards of ethical conduct.
- *Excellence.* The Finance Board strives for excellence in carrying out its responsibilities and recognizes the contributions of employees who demonstrate the highest professional standards in their work.

## GOAL 1

**GOAL 1.** The FHLBanks operate safely and soundly.

**OUTCOME 1:** FHLBanks identify and manage risk in an effective and efficient manner.

**OUTCOME 2:** FHLBanks remain adequately capitalized, and are able to raise funds in the capital markets.

## GOAL 2

**GOAL 2.** The FHLBanks serve the nation's housing finance and community investment needs.

**OUTCOME:** FHLBank funds are available for housing and community development by their members and housing associates in an effective and efficient manner.

## MEANS AND STRATEGIES

To carry out its mission, the Finance Board has one principal program: Supervision of the FHLBanks. Examinations are the cornerstone of the Finance Board's safety and soundness supervisory program. The performance, condition, and risk profile of each FHLBank is monitored through on-site examinations and other supervisory activities. The Office of Supervision is supported by the Offices of General Counsel and Management.

Means and strategies determine the processes, skills, technologies, and resources the Finance Board will use to achieve its strategic goals. They have a direct effect on the agency's overall efficiency and effectiveness. The following means and strategies are utilized:

### **Leverage resources to maximize supervisory oversight and regulatory activities.**

Finance Board staff has expertise in many disciplines including accounting, law, capital markets, lending, financial analysis, information technology, risk management, financial modeling community development, and affordable housing. An Examiner-In-Charge (EIC) is assigned to each FHLBank and draws on the knowledge and skills of other examiners and agency specialists when conducting supervisory activities.

### **Identify emerging risks and trends.**

Supervising the FHLBanks is a dynamic activity. At the close of each examination, the EIC, in consultation with other agency specialists, identifies key risks, including market, credit, and operational risks at a FHLBank, and develops a supervisory strategy for the upcoming year. The supervisory strategy allocates resources by risk area for an individual FHLBank.

### **Apply technology to enhance the effectiveness of the Agency.**

The Finance Board uses quantitative methods and financial models to provide analytic support to the

examination function. The agency assesses the market value and market value sensitivity of positions held by the FHLBanks, and focuses particularly on the positions with the greatest interest-rate sensitivity.

### **Sustain and improve organizational excellence.**

Organizational excellence is achieved through recruitment and retention of highly talented staff and development of staff's skills and knowledge. In recent years, the agency has established a performance-based pay system, increased staffing levels, and enhanced employee benefits. The Finance Board is committed to continually enhancing the performance, skills, and industry knowledge of its managers and staff. Through a variety of training opportunities, Finance Board staff enhances its skills, and stays abreast of developments in an evolving industry.

## STRATEGIC GOALS:

**GOAL 1:** *The FHLBanks operate safely and soundly.*

**OUTCOME 1:** The FHLBanks identify and manage risk in an effective and efficient manner.

### ANNUAL PERFORMANCE GOAL 1

*FHLBanks assessed as “Marginal” or “Unsatisfactory” improve their condition and/or practices.*

The level and direction of risk arising from the activities of the FHLBank and the quality of its risk management and corporate governance are assigned an overall conclusion category of Satisfactory, Fair, Marginal, or Unsatisfactory.

When the financial condition or performance, governance, operations, risk management practices and/or administration of the affordable housing or community investment programs warrant a heightened degree of supervisory concern, the FHLBank or the OF may be assessed as Marginal. The Finance Board uses informal supervisory actions to address the identified deficiencies or weaknesses.

The FHLBank or the OF may be assessed as Unsatisfactory when serious deficiencies exist in the financial, governance, operations, risk management practices and/or administration of the affordable housing or community investment programs. Formal supervisory actions are used to address these identified deficiencies or weaknesses. A formal supervisory agreement states the actions that the FHLBank must take to improve its overall performance and condition.

### ANNUAL PERFORMANCE GOAL 2

*FHLBanks operate in compliance with all supervisory agreements.*

The supervisory process is designed to identify and evaluate risks at the FHLBanks, assess compliance with statutes and regulations, and ensure that deficiencies are addressed in a timely manner. The Finance Board uses

formal and/or informal supervisory actions to correct deficient practices, conditions, or violations of law. When significant supervisory or compliance deficiencies, including violations of laws are identified, the Finance Board requires an action plan and/or supervisory agreement to address these deficiencies. Quarterly reviews, off-site monitoring, and subsequent annual examinations assess whether the FHLBank is operating in compliance with all supervisory agreements.

**OUTCOME 2:** FHLBanks remain adequately capitalized, and are able to raise funds in the capital markets.

## ANNUAL PERFORMANCE GOAL 1

*Each FHLBank operates at or above its minimum capital requirement.*

In December 2000, the Finance Board adopted a risk-based capital regime to complement its leverage capital regime. Risk-based capital requirements are imposed upon each FHLBank on the basis of the credit, market, and operations risks of that institution. FHLBanks must report its risk-based capital requirement by component amounts, as well as actual total capital amount and permanent capital amount, at least monthly to the Finance Board. The Finance Board monitors compliance with applicable capital requirements and evaluates capital management policies and procedures as part of the on-site examination of the FHLBanks. When a new capital structure plan has not been implemented, an FHLBank must adhere to the alternative leverage requirement in 12 C.F.R. § 966.3(a).

## ANNUAL PERFORMANCE GOAL 2

*Each FHLBank and the FHLBank System maintain a triple-A credit rating.*

The lowest cost credit is available to FHLBank members when the FHLBanks and the FHLBank

System maintain the highest possible credit rating. This rating allows the FHLBanks to issue consolidated obligations (the funding source for the FHLBanks' credit products) at terms that are competitive with other government sponsored enterprises (GSEs), and are only slightly higher than U.S. Treasury rates. FHLBank members use advances to finance long-term portfolio investments in residential mortgages, including affordable housing, and fund small business and agricultural loans.

**GOAL 2.** *The FHLBanks serve the nation's housing finance and community investment needs.*

**OUTCOME:** FHLBank funds are available for housing and community development by their members in an effective and efficient manner.

## ANNUAL PERFORMANCE GOAL 1

*The FHLBanks use funding and programs to support housing finance and promote community investment.*

Congress established the FHLBank System in 1932 to restore confidence in the nation's financial institutions and to improve the supply of funds to local lenders to finance loans for home purchases. The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 expanded the FHLBank System's public policy mission, and established the Affordable Housing Program (AHP) and a Community Investment Program (CIP).

The two major programs through which the FHLBanks provide funds to their members are secured loans (advances) and Acquired Member Assets (AMA). The FHLBanks make advances to their members to provide funds for residential housing finance and to provide funds to community financial institutions for small

businesses, small farms, and small agricultural businesses.

AMA is the comprehensive term for programs through which the FHLBanks acquire single-family mortgages, either whole loans or interests in whole loans, from participating members. AMA programs are structured such that a substantial portion of the credit risk is borne by the member. The FHLBanks' acquisition of loans from participating members is the functional equivalent of making an advance in that the member can access liquidity for additional mission-related lending.

The FHLBanks' use the AHP and CIP funds to support community and economic development activities of their members. The AHP subsidizes the cost of affordable owner-occupied and rental housing. The subsidy may be in the form of a grant or a below-cost or subsidized interest rate on an FHLBank advance to a member. Through the CIP, the FHLBanks provide funding to support the community and economic development activities of their members. By statute, each FHLBank must contribute at least ten percent of its net earnings from the previous year to the AHP, subject to a minimum annual combined contribution by all 12 FHLBanks of \$100 million.



# KEY EXTERNAL FACTORS

The Finance Board's direction, goals, and priorities are influenced by the environment in which the agency and the FHLBanks operate. Therefore, the Finance Board is taking action to improve its ability to assess emerging risks and develop alternatives to mitigate the impact of such risks. The agency has identified the following key areas that represent significant events, influences, and risks that may affect the Finance Board.

*Legislation:* Congress has been considering new legislation that would establish a single agency as the regulator for the GSEs that support the national housing market. This new agency would oversee the safety, soundness, and housing mission achievement of Fannie Mae, Freddie Mac, and the FHLBanks.

*Developments in Banking and Financial Markets:* Financial markets continue to evolve with new products and services introduced on a regular basis. These developments have the potential to affect, both positively and negatively, the demand for FHLBank products and services, and the FHLBanks' financial performance. As the industry evolves, the supervisory focus of the Finance Board also must be evolving to ensure continuous effective supervision of the FHLBanks. Recent matters under consideration include the FHLBanks' responsibilities regarding predatory lending by their members, accountability of officers and directors under the Sarbanes-Oxley Act of 2002, the potential for housing price decreases, increased foreclosure activity in areas affected by natural disasters, consolidation of the financial services industry, and the composition of FHLBank capital and the adequacy of retained earnings.

In addition, the rapid pace of technological innovation, especially in telecommunications and electronic data processing, continues to have a substantial effect on the economy of U.S. financial services. Harnessing technological innovations will create opportunities to improve the Finance Board's efficiency across organizational units and functions.

*Economic Variables:* During exceptionally adverse economic periods, *e.g.* high unemployment, decreasing housing prices, sharp or prolonged changes in interest rates, the financial condition of the FHLBanks may be significantly affected. The Finance Board is responding to strengthen the risk management practices or business operations of the FHLBanks to mitigate any identified weaknesses.

Staffing: In the competitive financial services environment highly skilled personnel are in great demand. That environment creates a continuing challenge for the Finance Board in recruiting and retaining a highly competent workforce. The Finance Board will respond appropriately to recruitment and retain examiners, economists, accountants, analysts, and attorneys with the requisite financial and technological skills to model, monitor, and assess the risks undertaken by the FHLBanks.

Continuity of Operations: Financial institutions must maintain a capacity to resume business after a crisis. Ensuring preparedness for a crisis continues to be a priority for the Finance Board, both its own operations as well as that of the FHLBanks and OF.

The Finance Board maintains an Emergency Operations Center (EOC) that has direct connectivity to all agency systems and provides essential personnel with the necessary resources to continue agency operations.

## STRATEGIC PLANNING PROCESS

To develop the fiscal year (FY) 2007-2012 Strategic Plan, representatives from all the Finance Board's Offices considered the financial condition of the FHLBanks, recent innovations in the banking industry, legislative developments, and issues affecting the FHLBank members and housing associates. Organizational considerations such as human capital, diversity management, financial resources, and technology were also included in the process.

The team crafted new measures that will be used to evaluate the Finance Board's ability to achieve its mission. While developing the Plan, the team conferred with agency leadership to discuss and establish agency priorities.

In developing the annual operating budget under the strategic framework, each Finance Board Office develops goals and objectives. The Office of Management reviews these budgets and resulting resource requests, and recommendations to the Board of Directors. The Chief Financial Officer and the Budget Officer provide support during the budget process.

# PROGRAM EVALUATION

The Finance Board uses program evaluations as an integral part of its effort to improve and enhance its mission performance and support strategic and performance planning efforts. These evaluations take many forms, and are performed by organizations both inside and outside the agency. Staff evaluates and implements recommendations, as appropriate. The principal evaluations include:

## **Supervisory Program**

*General Accounting Office (GAO) Evaluations:* The GAO conducts program- and program-support related evaluations of the agency's supervisory program.

*Office of Inspector General (OIG) Evaluations:* The OIG conducts independent evaluations of the agency's supervisory program and program support operations.

*FHLBank Strategic Planning Interview Project:* In 2005, the Finance Board held discussions with senior executives of each FHLBank to gather information about FHLBank practices and experiences in three major areas: (1) risk management and modeling; (2) financial reporting and data collection; and (3) information systems.

*Quality Assurance:* The OS is creating a Quality Assurance (QA) Program that will provide recommendations to facilitate efficient and effective operations. QA also will conduct *ex-post* reviews of all programs in the OS. These reviews may include, but will not be limited to, ongoing evaluation of work processes, policy development, and decision-making processes.

## **Financial Management**

*Financial Audits:* Annually, the OIG contracts with a public accounting firm to audit the Finance Board's financial statements. This audit is conducted in accordance with generally accepted auditing standards and Government Auditing Standards.

## **Information Technology**

*Federal Information Security Management Act (FISMA):* The OIG annually reviews and evaluates the agency's information technology systems for FISMA compliance. This includes evaluating information technology controls for financial management systems.

*Network Penetration:* Annually, the Finance Board contracts with an outside company of security experts to perform network penetration testing of our information technology systems.

*Customer Satisfaction Survey:* Annually, the Finance Board conducts a survey of all end-users to obtain their opinions on the quality of the agency's products and services. This allows a better understanding of user needs and improved service.

### **Human Capital Management**

*Human Capital Management Survey:* Annually, the Finance Board participates in the Office of Personnel Management's Human Capital Management Survey. Recommendations are evaluated and implemented, as appropriate.

*Training and Development Program:* The Finance Board is committed to training and development of its staff to build, maintain, and improve individual and team competencies to meet the demands and challenges of today as well as of the future in the financial and regulatory arenas. A more formalized training and development program is underway in the Office of Supervision that will address a variety of training and development opportunities through various activities and forums. Undertaking a particular training or development activity will be considered based on the needs in acquiring new skills or enhanced performance.

*Workplace Improvement Committee:* Representatives from all offices within the Finance Board meet to identify and pursue improvements to the Finance Board's work environment.

*Equal Employment Opportunity (EEO):* The Finance Board is committed to equal employment opportunity and the implementation of a strong EEO program to promote employment and advancement opportunities without regard to race, sex, sexual orientation, religion, color, national origin, age or disability. The Minority and Disabled Recruitment Task Force, comprising staff from a cross-section of Offices and disciplines within the Finance Board, meets periodically and discusses strategies for

enhancing recruitment initiatives to attract a diverse applicant pool. In addition, the Finance Board is committed to continuing to take advantage of employment programs that integrate veterans, disabled, and other populations into the public sector workforce.